No. 75-1889

In the Supreme Court of the United States

OCTOBER TERM, 1976

COMMONWEALTH OF PENNSYLVANIA AND
NEW YORK STATE DEPARTMENT OF TRANSPORTATION,
PETITIONERS

v.

INTERSTATE COMMERCE COMMISSION AND
UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE UNITED STATES AND THE INTERSTATE COMMERCE COMMISSION IN OPPOSITION

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-21a) is reported at 535 F. 2d 91. The regulations of the Rail Services Planning Office of the Interstate Commerce Commission and the supporting reports (Pet. App. 24a-57a) are published at 40 Fed. Reg. 1624 and 40 Fed. Reg. 14186.

JURISDICTION

The judgment of the court of appeals (Pet. App. 22a-23a) was entered on March 31, 1976. The petition for a

writ of certiorari was filed on June 29, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES INVOLVED

Section 205(d)(6) and Section 304(c)(2)(A) of the Regional Rail Reorganization Act of 1973, 87 Stat. 994, 1008-1009, as amended by Sections 309 and 804 of the Railroad Revitalization and Regulatory Reform Act, Reform Act, (P.L. 94-210, 90 Stat. 59, 135), 45 U.S.C. 715(d) Pub. L. 94-210, 90 Stat. 58-59, 134-135,[1] are set forth at pages 3 and 5-6 of the petition.

QUESTION PRESENTED

Whether regulations of the Rail Services Planning Office of the Interstate Commerce Commission defining the term "avoidable costs" conform to Section 304(c)(2)(A) of the Regional Rail Reorganization Act.

STATEMENT

The Regional Rail Reorganization Act of 1973 (the "Rail Act"), 87 Stat. 985, 45 U.S.C. (Supp. V) 701 *et seq.*, as amended by the Railroad Revitalization and Regulatory Reform Act of 1976 ("the Reform Act"), Pub. L. 94-210, 90 Stat. 31, provides for the reorganization of eight major northeastern and midwestern railroads, under a final system plan, into a single viable system consisting of rail properties designated for transfer to a private-for-profit corporation. *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 109.[2] The carriers' rail properties not designated for transfer are subject to a

[1]Unless otherwise noted, section references throughout will be to the Rail Act as amended by the Reform Act.

[2]The final system plan became effective on November 9, 1975, and designated rail properties were conveyed on April 1, 1976. Sections 208(a) and 303(b).

secondary planning and reorganization process. The carrier may discontinue service and dispose of such properties (*Regional Rail Reorganization Act Cases*, *supra*, 419 U.S. at 116-117; Section 304(a) and (b)), *unless* a financially responsible person (which may be a government entity) offers to subsidize service by providing a rail service continuation payment under Section 304(c) of the Act. If the offer covers the difference between the "revenue attributable" to such rail properties and the "avoidable costs" of providing rail service on such properties,[3] together with a "reasonable return" on the value of such properties, the rail service involved may not be discontinued or abandoned. Section 304(c)(2)(A). This provision is the cornerstone of the State and Local Rail Services Continuation Program embodied in Title IV of the Rail Act, Sections 401-403.[4]

Section 205(a) of the Rail Act established the Rail Services Planning Office ("RSPO") in the Interstate Commerce Commission. Section 205(d)(3) of the original Act required RSPO, by rulemaking, to "determine and publish standards for determining the 'revenue attributable to the rail properties,' the 'avoidable costs of providing service,' and 'a reasonable return on the value,' as those phrases are used in section 304 of this Act." 87 Stat. 994. Section 304 used those terms only in connection with rail service continuation subsidies. 87 Stat. 1008-1009.

[3]*I.e.*, avoidable by termination of service.

[4]Under that Program, each State in the region is entitled to receive rail service continuation subsidy assistance (Section 402) and acquisition and modernization loans (Section 403) for purposes of continuing rail services pursuant to State plans for rail transportation and local rail services (Section 402(c)(1)) under regulations issued by the Secretary of Transportation (Section 402(c)(4) and (d)). These regulations have been issued and are codified at 49 C.F.R. Part 255.

Pursuant to that mandate, on February 25, 1974, RSPO issued a notice of proposed rulemaking and order (39 Fed. Reg. 7182). After an extended period for public comment, RSPO issued initial standards on July 1, 1974 (39 Fed. Reg. 24294) and, after further comment and field testing,[5] issued amended standards on January 8, 1975 (Pet. App. 24a-46a), and adopted its present regulations on March 28, 1975 (Pet. App. 49a-57a).[6]

In order to fashion a subsidy formula that would leave room for "arm's-length negotiations between the parties," yet assure the continuation of needed service by providing a "mandatory procedure" in the event that agreement could not be reached on a voluntary basis (Pet. App. 25a-26a), RSPO first sought to develop a method for ascertaining the "revenue attributable" to particular rail properties. Because it was unable to construct what it considered to be an appropriate basis for allocating rail freight revenues to branch line operations (Pet. App. 31a), RSPO defined "revenue attributable" to such operations to include *all* system revenues earned on freight traffic *either* originating *or* terminating on the branch line, together with an allocation of passenger revenue based on the ratio of

[5]All interested parties were invited to participate through publication of notice of the proposal in the Federal Register and by service upon all parties of record in the rulemaking proceeding (39 Fed. Reg. 33574). See discussion in January 8, 1975, report (Pet. App. 26a).

[6]RSPO allowed 113 days for public comment, during which it received and evaluated more than 300 statements, before it issued its initial standards (39 Fed. Reg. 19362). The amended standards reflected experience in tests conducted at the Penn Central data collection headquarters in Philadelphia, and on two Penn Central branch lines; public seminars conducted during August and September of 1974; and comments seeking revision of the initial standards (Pet. App. 25a). Only seventeen additional comments were received after promulgation of the amended standards (Pet. App. 50a).

passenger car miles on the branch to passenger car miles on the system of railroad, to the extent such revenue is earned by passenger trains originating or terminating on the branch line (49 C.F.R. 1125.4; Pet. App. 39a-40a, 57a).[7]

This allocation of system revenues to the branch line affected the definition of "avoidable costs" identified with the production of those revenues. RSPO agreed with petitioners that "avoidable costs" should be strictly construed (Pet. App. 31a). However, it recognized that a narrow construction of that term does not necessarily preclude consideration of "indirect costs" (*ibid.*). Since related off-branch revenues were attributed to the branch lines, related off-branch costs were also properly attributable under the definition of "avoidable costs." RSPO stated (Pet. App. 33a):

[7]RSPO's decision to include all revenue earned on freight traffic either originating or terminating on the branch line represented a departure from the formula traditionally employed by the Commission in abandonment proceedings under Section 1(18) of the Interstate Commerce Act, as added and amended, 41 Stat. 477, 49 U.S.C. 1(18). That formula allocates revenue earned on freight moving over the branch line between the branch and the system, with 50 percent of the system revenue then added to the branch. Cf. *Penn Central Co. Abandonment*, 347 I.C.C. 223, 225. However, RSPO recognized that the circumstances underlying discontinuance of service and abandonment of rail properties under Section 304 of the Rail Act "are not analogous to those involved either in an abandonment proceeding under section 1(18) of the Interstate Commerce Act or in the determination of a reasonable return on an investment base necessary for the continuing discharge of common carrier obligations in the public interest" (Pet. App. 34a; see also, Pet. App. 53a), and no significant objections were raised to RSPO's definition of "revenues attributable" as finally promulgated. Petitioners here challenge only RSPO's definition of "avoidable costs" insofar as that definition includes certain elements of so-called "off-branch costs," and specifically state that they "do not quarrel with the [definition of] 'revenue attributable' " (Pet. 6).

> While on the surface it might seem inconsistent to allow system variable costs to be allowed for off-branch costs, it is believed justified on the basis of equity to the railroad since all system revenues from traffic originating or terminating on the branch are attributed to the branch. A failure to recognize off-branch variable costs would probably lead to situations where the operating railroad would try to divert the traffic to another carrier at the earliest possible point regardless of service considerations. This would not only result in circuitous movement and concomitant time delays but would also decrease the revenue attributable to the branch. The adopted approach recognizes the services rendered by the carrier to the branch traffic.

Accordingly, the regulations define the "avoidable costs of providing service" to include all costs associated with handling freight traffic or providing passenger service on the branch line itself (on-branch costs) (49 C.F.R. 1125.5(a)-(j); Pet. App. 40a-44a, 57a) and, in addition, with respect to freight traffic only, certain costs associated with handling traffic originating or terminating on the branch line to the extent that such traffic moves over the remainder of the railroad's system (off-branch costs) (49 C.F.R. 1125.5(k); Pet. App. 44a).

In adopting this approach, RSPO recognized that off-branch costs would not be considered "avoidable" costs in an ordinary abandonment proceeding. It determined, however, that abandonment standards are not a valid comparison because "[t]he subsidy standards are designed in accordance with the Act to define the cost of providing service and not the cost of abandoning service" (Pet. App. 53a). The Office likewise rejected the contentions that more sophisticated bases for calculating off-branch

costs were necessary, finding that the costs associated with the installation of a systemwide cost accounting and reporting system "[could] not be justified on the basis of the subsidy program alone" (Pet. App. 29a) and that use of a system based on per diem regulations to develop car costs would be "overly complex to apply" (Pet. App. 54a).

On petitions for review,[8] petitioners contended that RSPO erred in failing to follow abandonment standards, and also argued, for the first time, that RSPO was foreclosed from adopting a definition of "avoidable costs" that attributed any portion of off-branch costs to the branch line because of the Commission's interpretation of the identical phrase in regulations issued under Section 401 of the Rail Passenger Service Act of 1970, 84 Stat. 1334, 45 U.S.C. 561 ("Passenger Act").

The court of appeals, in a unanimous opinion by Judge Leventhal, rejected these contentions. It held that the legislative history of the statute did not show any congressional intent that avoidable costs "be measured by duplication of the ICC regulations under the 1970 law" (Pet. App. 9a). It agreed with RSPO that the Rail Act, with its focus on subsidized continuation of service, had a different purpose from that of both the old abandonment statute and the Passenger Act (Pet. App. 5a-9a). The court emphasized that the Rail Act required only "a clear nexus between the revenues

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[8]The statute makes no provision for administrative review by the Commission of RSPO's regulations under the Act. Nevertheless since RSPO was established as an office in the Commission (Section 205(a)), its regulations were deemed to be regulations of the Commission for purposes of judicial review under 28 U.S.C. (Supp. V) 2321.

attributable to the particular line and the costs incurred in their production" (Pet. App. 9a, n. 6a) and held that RSPO's regulations established that nexus (Pet. App. 11a). Accordingly, after finding that "[t]he opposing States * * * have not shown that RSPO's approach will require a significantly greater expenditure of state revenues for rail service continuation subsidies than the approaches they advocate" (Pet. App. 11a), the court rejected "the contention of the petition filed by the States that the RSPO regulation is facially invalid, without prejudice to reconsideration in light of a particularized factual showing as to the consequences of the regulation" (Pet. App. 11a).[9]

ARGUMENT

The decision of the court of appeals is correct and does not warrant review by this Court.

1. The Rail Act embodies "imaginative and innovative solutions" to a developing crisis. *In re Penn Central Transportation Co.*, 384 F. Supp. 895, 904 (Special Rail Act District Court). One such solution is a major shift in national railroad policy by which unprofitable lines may be continued in operation under state-federal subsidies, rather than simply abandoned by the railroads (Pet. 12). The measure of the subsidy is the difference between the "avoidable cost" of service and the "revenue attributable" to it, plus a reasonable return. Petitioners, as States that offer such subsidies, are interested in reducing them by keeping "avoidable costs" low and "attributable revenues" high. They contend

[9]The court also held (Pet. App. 3a-4a) that a challenge by another party to the constitutionality of the Act could be determined only in the special Court created under Section 209(b) of the Rail Act, 87 Stat. 999-1000, as a result of amendments to its jurisdiction made by Section 602(b) of the Reform Act, 90 Stat. 86-87.

therefore that RSPO erred in permitting "avoidable costs" to be enlarged, for subsidy purposes, by certain off-branch costs. The court of appeals correctly recognized that the definition, on its face, comes within the broad discretion conferred on the agency by Congress.

Petitioners contend that in enacting the Rail Act Congress meant "avoidable cost" to have the precise meaning attributed to the term by the Commission in its regulations under the Passenger Act (Pet. 12-13).[10] But the Act's provisions for subsidized continuation of service furnished a new alternative to abandonment of failing branch lines or (as with the Passenger Act) their transfer to a government-sponsored corporation. In making such a major policy innovation, Congress could scarcely have intended to bar corresponding innovation in the rules that give life to the Act's policy.[11]

The pertinent language of the Rail Act, as amended by the Reform Act, itself shows that Congress did not intend RSPO to be bound by prior formulations under other statutes. Section 205(d)(3) of the original Rail

[10]Those regulations, issued in a proceeding entitled Ex Parte No. 268, *Determination of Avoidable Losses under the Rail Passenger Service Act of 1970*, 343 I.C.C. 379, are codified at 49 C.F.R. Part 1123 and governed the payments required of carriers in exchange for relief from their statutory obligation to provide passenger service.

[11]Experience has indicated the workability of the standards developed by RSPO. Fourteen States, including both New York and Pennsylvania, have entered into rail service continuation operating agreements based upon the standards promulgated by RSPO. In total 204 branch lines involving 3,111 miles of track, including 90 branch lines and 1093.5 miles of track in New York and Pennsylvania, are being operated under such agreements.

Act (87 Stat. 994) directed RSPO to "determine and publish standards for determining the 'revenue attributable to the rail properties,' the 'avoidable costs of providing service,' and a 'reasonable return on the value' * * *," as those terms were used in Section 304 to define the coverage of rail service continuation subsidies for properties not designated in the northeast region final system plan. This mandate was further enlarged by Section 309 of the Reform Act, which added Section 205(d)(6) to the Rail Act (90 Stat. 58-59). The amendment not only restated RSPO's prior responsibility to define "avoidable costs" and related terms as used in Section 304, but also directed it "from time to time [to] revise and reissue standards" for determining them. This language clearly imposes a dynamic responsibility, not a static codification of earlier concepts. Cf. *Permian Basin Area Rate Cases*, 390 U.S. 747, 776.

As petitioners note (Pet. 12), the regulations implementing the Passenger Act had already been published when Congress passed the Rail Act; had Congress meant these regulations to apply under the latter law, it could easily have said so. Instead, Congress gave the new office general authority, to be exercised after rulemaking, to "determine and publish standards for determining" avoidable cost and other key terms. 87 Stat. 994. And while the legislative history shows that Congress did not leave the matter entirely open-ended,[12]

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[12]The Senate Report stated:

> While the Commission would determine and publish the standards for calculating the revenues attributable to the rail properties and the avoidable costs of providing service, the Committee expects the Commission to define avoidable costs in such a way as to allow the Corporation or other person performing the service to recover all costs directly attributable or solely related to the costs of a particular service, but would not include any portion of common costs which *operation of a line*. [Emphasis added.]

S. Rep. No. 93-601, 93d Cong., 1st Sess. 37 (1973).

that history, as the court of appeals pointed out, does not indicate that these costs should or must be measured by the Commission's regulations under the Passenger Act (Pet. App. 9a).

What the legislative history does show (n. 12, *supra*) is a congressional intention that, whatever definition might be chosen, there be "a clear nexus between the revenues attributable to the particular line and the costs incurred in their production, to exclude 'any portion of the common costs which would not be covered by revenues received by operation of a line' " (Pet. App. 9a, n. 6a). RSPO's definition meets this test. After extensive study (Pet. App. 25a-26a), RSPO concluded that it was unable to separate the on-branch from off-branch revenues of a line, and thus ruled that a line would be credited with all revenue accruing from traffic which originates or terminates on the line (Pet. App. 31a, 40a).[13] Since RSPO was including off-branch revenue in its "revenue attributable" standard, it reasoned that in the interest of fairness and efficiency that some off-branch costs should be included (Pet. App. 33a). RSPO carefully chose costs that contribute to the production of the pertinent revenue: terminal and/or interchange costs, and line-haul costs

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[13]Petitioners do not challenge this definition, which is to their advantage (Pet. 6). The formula also calls for the addition of an allocation of passenger revenue, but, in view of the very limited nature of passenger service, this element is not important, and is not in dispute here.

(Pet. App. 33a). Thus, as the court of appeals held (Pet. App. 9a, n. 6a), RSPO's formula establishes the required "nexus" between costs and revenue.

Since RSPO faithfully discharged its statutory duty in defining the terms set forth in the Rail Act, there is nothing to petitioners' suggestion that its regulations impermissibly differ from those defining the terms under other statutes (Pet. 15). An agency has the authority to change prior interpretations of the same statute, provided it gives a reasoned explanation for doing so. *American Trucking Associations, Inc.* v. *Atchison, T. & S.F.R. Co.*, 387 U.S. 397, 416; *Atchison, T. & S.F.R. Co.* v. *Wichita Board of Trade*, 412 U.S. 800, 808. The agency's latitude is much greater when it offers a different interpretation of a phrase common to separate statutes with different histories and purposes. As the court of appeals recognized (Pet. App. 6a-10a), regulations issued under the old abandonment statute and the Passenger Act do not affect the validity of different regulations under the Rail Act. Moreover, the construction of the statute by RSPO (Pet. App. 8a-9a), as the agency charged by Congress with setting the new administrative machinery in motion, is entitled to great weight. *Udall* v. *Tallman*, 380 U.S. 1, 16; *Train* v. *Natural Resources Defense Council*, 421 U.S. 60, 67, 75.

Since Congress did not bind RSPO to adopt the standards for "avoidable costs" developed in abandonment cases under prior law, petitioners' contention (Pet. 12-14) that there cannot be one definition of "avoidable costs" for subsidy purposes and another for abandonment purposes is beside the point. RSPO's present standards for purposes of service continuation subsidies under the original Rail Act may or may not prove suitable for discontinuance or abandonment purposes under the amended Rail Act, or under the changes in the Interstate Commerce Act adopted in the Reform Act. This

is a matter to be explored in future joint rulemaking by RSPO and the Commission, subject to judicial review on petition by those aggrieved.[14]

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[14]Section 304(a)(2)(A), added to the Rail Act by Section 804 of the Reform Act (90 Stat. 133-134), provides that rail service may be discontinued on rail properties not included in the northeastern region final system plan, and not otherwise designated for use under the Rail Act, "if the Commission determines that such rail service on such rail properties is not compensatory * * *." For purposes of this provision, the statute provides that service is compensatory if revenues attributable to the line equal or exceed avoidable costs plus a reasonable return on the value of the properties, "as determined in accordance with the standards developed [by RSPO] pursuant to section 205(d)(6) of this Act." Section 304 (a)(2)(B), 90 Stat. 134. The Commission is therefore responsible for determining when service is compensatory, and RSPO for defining the statutory terms.

But the fact that the Commission may be called upon to apply RSPO standards developed for subsidy computation purposes in passing upon applications for authority to discontinue service under Section 304(a)(2) does not, as petitioners contend (Pet. 13), demonstrate that such standards are inappropriate for the purpose for which they were developed. In any event, no applications for authority to discontinue service under this provision have been filed to date and few, if any, are anticipated prior to its expiration on November 9, 1976 (Section 304(a)(2)(A)(ii)).

While the provisions of amended Section 304(a)(2) apply only to a few of the lines in the northeastern region subject to the Rail Act, Section 802 of the Reform Act amends the procedure for discontinuances and abandonments of lines in other parts of the country. A new Section 1a has been added to the Interstate Commerce Act, which provides for discontinuance and abandonment and for the continuation of rail freight service, if financial assistance is offered which covers the difference between "revenues attributable" to the line and "avoidable costs", plus a reasonable return. 90 Stat. 127-130. As used in this provision, "avoidable costs" is defined by the statute to mean "all expenses which would be incurred * * * in providing a service which would not be incurred * * * if such service were discontinued or * * * if the line * * * were abandoned." Section 1a(10), 90 Stat. 130. The Commission, not RSPO, is responsible for applying the formula to calculate the net of "avoidable costs" plus

2. There are additional reasons that render further review inappropriate at this time. The court of appeals correctly found (Pet. App. 11a) that petitioners had failed to establish that RSPO's standards will require a "significantly greater" expenditure of state funds for rail service continuation subsidies than the approaches they advocated.[15] Moreover, the court made clear that petitioners will be entitled to reconsideration if they can make a particularized factual showing regarding adverse consequences resulting from RSPO's revenue-cost formulation as applied. Following any such reconsideration, the issues could be considered on the basis of "a much more developed record" confined to "particular situations." Cf. *Regional Rail Reorganization Act Cases, supra,* 419 U.S. at 146, and cases cited therein.

"return on value" over "revenues attributable" for subsidy purposes (Section 1a(7), 90 Stat. 129), although RSPO retains responsibility for defining avoidable costs for purposes of Section 1a under Section 205(e)(1)(B) of the Rail Act, as added by Section 309 of the Reform Act (90 Stat. 59).

[15]It is also by no means clear that RSPO's approach will require an expenditure *any* greater than that which would have been required had the Commission's traditional revenue/cost formulation been adopted. Under the traditional formulation used in abandonment cases only 50 percent of the revenues earned on traffic moving beyond the branch line would be attributed back to the branch line, the remainder being deemed to be absorbed by costs associated with handling the traffic over the balance of the system. Under RSPO's formulation, on the other hand, all of the revenues are attributed to the branch line and an attempt is made to ascertain the costs incurred by the system in earning those revenues. While the latter approach should result in a more accurate allocation of costs and revenues, there is no basis at present for asserting with confidence that one or the other approach increases the amount of subsidy required to provide for continued branch line operations. Petitioners would apparently favor recognition of all of the revenues and none of the costs associated with operations beyond the branch line (Pet. 6), but such an approach would plainly be unfair to the subsidized railroad.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER 1976.

DOJ-1976-09